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In The

Supreme Court of the United States

October Term, 1984

TEXAS OIL & GAS CORPORATION,

Petitioner,

v.

ARKLA EXPLORATION COMPANY,
STATE OF ARKANSAS, and
WILLIAM P. CLARK, Secretary of
the Department of Interior,

Respondents.

On Petition For Writ of Certiorari
to the Eighth Circuit Court of Appeals

BRIEF AMICUS CURIAE OF MOUNTAIN STATES LEGAL FOUNDATION, ROCKY MOUNTAIN OIL AND GAS ASSOCIATION, AND INDEPENDENT PETROLEUM ASSOCIATION OF MOUNTAIN STATES

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With the written consent of all parties, the Mountain States Legal Foundation (MSLF or Foundation) respectfully submits this brief as amicus curiae on behalf of its members, the members of the Rocky Mountain Oil and Gas Association (RMOGA), and the members of the Independ-

ent Petroleum Association of Mountain States (IPAMS), Amicus has filed the consents of all parties with the Clerk of the Court.

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INTEREST OF AMICUS CURIAE

MSLF is a nonprofit, membership, public interest law foundation dedicated to bringing before the courts those issues vital to the defense and preservation of individual liberties, private property rights, and the free enterprise system. The Foundation seeks to protect the vested property rights of its members, including their rights in federal oil and gas leases.

RMOGA is a voluntary, nonprofit association whose purpose is to promote the discovery, development, production, and conservation of oil and gas in the Rocky Mountain region. RMOGA's 600 members are involved in all phases of the oil and gas industry and related businesses. RMOGA is unique in that it represents all facets of the industry from the oil field to the service station.

IPAMS is a voluntary nonprofit association whose purpose is to represent the interests of 1700 independent oil and gas producers in the Rocky Mountain region. Its 1700 members, including producers and related support companies, seek to promote the exploration, development, and production of oil and gas in the mountain states.

The instant case is of particular importance to the members of MSLF, RMOGA, and IPAMS. Each organization has members who have qualified for federal oil and

gas leases under the noncompetitive leasing program by complying with the Mineral Leasing Act of 1920 and the regulations of the Department of Interior for oil and gas lease applications. The Eighth Circuit decision upheld the revocation of leases that were also issued in accordance with the Mineral Leasing Act and the regluations. The court declared the Interior Department's definition of a known geologic structure unlawful, and thus, leases issued using that definition may be subject to challenge.[1] As a result, the members of MSLF, RMOGA, and IPAMS are faced with the possibility that now or in the future the Department of Interior will rely on the *Arkla* decision to review KGS determinations. This uncertainty can have great detrimental effect in an industry that requires great capital outlays and relies on certainty.

SUMMARY OF REASONS FOR GRANTING THE WRIT

The Eighth Circuit Court's decision in *Arkla Exploration Co. v. Texas Oil & Gas Corp.*, 734 F.2d 347 (8th Cir. 1984) creates new law by adding market forces, such as competitive interest and exploration risk, to the Department of Interior's sixty year old definition of a known

[1]The Amicus organizations do not believe that the Department of Interior or a third party can legally contest a lease already issued in accordance with the law. However, even the possibility of that action has such serious consequences for the oil and gas industry that the Amicus organizations believe that this Court needs to resolve the issue now in favor of the security of lease title.

geologic structure (KGS).[2] By introducing these factors into the Interior Department's decision of whether the federal lands should be leased competitively, the Eighth Circuit's opinion assumes the role of a judicial legislature and changes what Congress has declined to change. As a result of this judicial change, serious questions are raised as to the status of leases issued under the disapproved definition or as to leases issued thereafter.

In concluding that the Department of Interior's KGS standards conflicted with the Mineral Leasing Act, the Eighth Circuit ignored the fact that the statutory review period of 90 days had long expired before Arkla Exploration Company sought relief in the Arkansas federal courts. This raises two very important questions—whether existing leases can be reviewed under the new KGS criteria and whether future noncompetitive leases are left open to revocation upon a KGS determination. This possibility creates unwelcome uncertainty in lease title that has far reaching consequences for the entire oil and gas industry.

This brief Amicus Curiae will demonstrate how the Eighth Circuit's holding may affect the status of thousands of noncompetitive leases. The administrative uncertainty about lease title will in turn impair the nation's long term efforts to find and develop onshore oil and gas.

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[2]This definition determines whether federal lands are leased on a competitive or noncompetitive basis. The Mineral Leasing Act of 1920 (MLA) provides that federal lands within a geologic structure known to contain oil or gas deposits shall be leased to the highest qualified bidder after competitive bidding. 30 U.S.C. § 226(b) (1982). Federal lands not deemed to be located in a KGS may be leased to the first qualified applicant under the noncompetitive leasing program. 30 U.S.C. § 226(c) (1982).

For more than 60 years, a lessee whose application for a federal lease was accepted could be certain that the lease was his for the statutory term. This security of title is an essential prerequisite for the exploration and development of oil and gas. Without such certainty the lessee will be reluctant to drill wells if he cannot be certain that the lease is his.

This decision comes at a time when energy independence remains an important policy objective of the United States. Noncompetitive leases account for an estimated 75 percent of the onshore lease activity on federal lands. If these leases lose their presumption of validity, the nation may lose potential production and revenues of substantial magnitude. Energy independence played an important role in the formulation of the noncompetitive leasing program in 1920 and has continued to be of paramount importance.[3] Clearly, the effect of the Eighth Circuit decision runs counter to the very law that it purports to uphold.

DISCUSSION OF REASONS FOR GRANTING THE WRIT

A. The Eighth Circuit Decision Rewrote The Definition Of A Known Geologic Structure

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[3]In 1935, Congress repealed the noncompetitive program, but reenacted it in 1946, because the nation's war experience demonstrated a continuing need to stimulate the discovery of new energy reserves and to grant incentives to persons exploring for unproven wells. S. 1236, 79th Cong., 2d Sess., 92 *Cong. Rec.* 9102 (1946).

By Requiring The Interior Department To Consider Competitive Interest And Exploration Risks.

The ruling in *Arkla Exploration Co. v. Texas Oil & Gas Corp.*, 734 F.2d 347 (8th Cir. 1984), stunned the nation's oil and gas industry. Prior to 1983, no court or administrative proceeding had ever held that the agency had to take into account competitive interest or the risks of exploration when defining a KGS.[4] The inconsistencies between what the court held and the agency's definition (which has not been changed over the sixty year period that it has been in use) create doubt about the certainty of title to noncompetitive leases, once they have been formally issued by the Secretary of the Department of Interior.

Specifically, the Eighth Circuit held:

> Perhaps even more serious than the Secretary's failure to make use of the available geologic data and expertise is his failure to consider actual competitive interest in the Fort Chaffee area shown by Arkla and other oil companies.

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[4]None of the cases cited by the Eighth Circuit or the district court support the holding that competitive interest or exploration risks must be considered in deciding whether a given area of land falls within a known geologic structure. *Hepburn T. Armstrong*, 72 IBLA 329 (1983) (holding that "The fact that oil companies active in the area have expressed no interest in the lands at issue does not undermine Survey's KGS designation."); *Nola Grace Ptasynski, Barbara C. Lisco*, 19 IBLA 125 (1975) (affirming the USGS KGS classification despite acknowledged risks and uncertainties of the geology.); *John P. Dever*, 67 Interior Dec. 367 (1960) (quoting the USGS Circular 419 (1959) which only cites physical geologic characteristics as factors to be considered in the KGS determination procedure).

Arkla Exploration Co. v. Texas Oil & Gas Corp., 734 F.2d at 360.[5] In attacking the Department of Interior's internal review of the KGS classification, the court further stated:

> Thus, the USGS's own study reveals that competitive interest and risk of exploration were not considered in making the Fort Chaffee KGS determinations. Because relative risk of exploration and exploration interest lie at the heart of the competitive/noncompetitive leasing dichotomy in the MLA, the failure of the USGS and the Secretary to consider these factors renders the KGS determination unlawful.

Id. at 360-61.

A comparison of the above holdings with the actual language of the statute and the regulations demonstrates how far the Eighth Circuit strayed from the legislation in question. Section 17 of the Mineral Leasing Act of 1920 provides in pertinent part:

> (c) If the lands to be leased are not within any known geological structure of a producing oil or gas field, the

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[5]The district court held in part that:

> In making any future KGS determintions, the following factors, among others, need to be considered: the Congressional intent in exploration and development of areas in which the exploration interest is relatively slight and the risk relatively great; the Congressional intent to promote competition in those areas wherein exploration interest is already present and the risks substantially less; . . . in determining and applying the true definition of the term "known geologic structure" consistent with Congressional intent, the clearly expressed Congressional purpose in providing the State of Arkansas and its counties and schools with a "fair" return on the value of the lands and minerals acquired from the State of Arkansas by the federal government, should be considered.

Arkla Exploration Co. v. Watt, 562 F. Supp. 1214, 1227 (W.D. Ark. 1983).

> person first making application for the lease who is qualified to hold a lease under this Act shall be entitled to a lease of such lands without competitive bidding.

30 U.S.C. § 226(c) (1982).

The regulations follow the legislative language and provide:

> A known geologic structure is technically the trap in which an accumulation of oil or gas has been discovered by drilling and determined to be productive, the limits of which include all acreage that is presumptively productive.

43 C.F.R. § 3100.0-5. (1984).

In conclusion, a review of Section 17 of the MLA demonstrates that the court amended the law by judicial decision making and that Interior's failure to consider such factors as competitive interest or exploration risks is not unreasonable. The statutory phrase "structures known to contain deposits of oil or gas" only refers to the geology of the land in question. The Eighth Circuit's factors concern market forces that are extraneous to the land's geologic characteristics and clearly write new law.

B. The Arkla Decision Could Affect The Lease Title Of Thousands Of Noncompetitive Leases.

Prior to the *Arkla* decision in the Eighth Circuit, once a lease was issued under the MLA and the regulations, it was presumed to be valid. *See Union Oil Co. of California v. Morton,* 512 F.2d 743 (9th Cir. 1975). However, following the *Arkla* decision, there is no such certainty. The court did not merely find that the TXO leases should not

have been issued under the noncompetitive program. Instead, the court held that the agency procedures to define a KGS conflicted with the MLA and that the agency must take into account a number of factors when defining a KGS that heretofore have never been considered, namely exploration risk and competitive interest.

While the court may have believed that such factors are relevant to the noncompetitive leasing program, the fact remains that the court invalidated Department of Interior standards that have been the basis of issuing noncompetitive leases for more than half a century. Since the court held that the agency standards were contrary to the MLA, there is a real possibility that other existing noncompetitive leases may be subject to challenge as having not been leased in accordance with the law.[6] Even if the decision is not applied retroactively, the possibility of future leases not having the certainty that title vests will impair future efforts to find oil and gas.

The impact of the *Arkla* decision on other lessees is amply illustrated by what happened to Texas Oil and Gas Corp. The company fully complied with both the Mineral Leasing Act of 1920 and the regulations of the Department of the Interior in filing applications for noncompeti-

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[6]The Secretary has the power in an administrative proceeding timely initiated to cancel a lease of public lands issued in contravention of the provisions of the Mineral Leasing Act. Until the *Arkla* decision, this power was limited. "We sanction no broader rule than is called for by the exigencies of the general situation and the circumstances of this particular case. We hold only that the Secretary has the power to correct administrative errors of the sort involved here by cancellation of leases in proceedings timely instituted by competing applicants for the same land." *Boesche v. Udall,* 373 U.S. 472, 485 (1963).

tive gas leases on acquired military lands. After more than five years of litigation, the Eighth Circuit held that the leases were issued contrary to the MLA and were therefore properly revoked.

This result clearly falls outside the recognized limits on the cancellation of leases. Arkla Exploration Co. never filed lease applications for the land and allowed its administrative challenge of the lease to lapse. By upholding Arkla's contest, the court opens the door for other lease challenges that do not meet the previously recognized limits on cancellation of noncompetitive leases. 30 U.S.C. § 226-2 (1982). Therefore, the Eighth Circuit has established legal precedent that threatens the possible revocation of other noncompetitive leases issued under similar "defective" KGS classifications. For these reasons, the members of MSLF, RMOGA, and IPAMS are concerned that the rules by which they have done business have been thrown out and that their property rights as federal lessees have been diminished.

C. The Arkla Exploration Co. Decision May Reduce Oil And Gas Exploration And Production.

The noncompetitive lease program for public and acquired lands plays a major role in the exploration and development of domestic reserves of oil and gas. Its health is especially important to the small, independent operator, without the financial resources of the major oil companies to bid for competitive leases. These small operations account for 90% of the "wildcat" drilling aimed at discovering new sources of oil and gas.

An estimated 75% of the federal onshore oil and gas leases are issued under the noncompetitive leasing pro-

gram. During Fiscal Year 1983, a total of 11,469 noncompetitive oil and gas leases affecting 18,247,476 acres of federal land (public domain and acquired lands) were issued by the Bureau of Land Management.[7] As of September 30, 1982 there were a total of 115,389 continuing oil and gas leases (both competitive and noncompetitive) on the public lands[8] and 14,492 continuing oil and gas leases on acquired, military, and other federal lands.[9]

Because the noncompetitive lease program plays a major role in domestic petroleum activity, it also accounts for a substantial part of the nation's onshore petroleum production. From 1950 to 1983, oil production from federal and Indian leases represented 13.2 percent of the total United States production. In 1983 alone, it represented 16.2 percent of that total production.[10]

The noncompetitive program plays an even greater role in gas production totals. From 1950 to 1983, gas production from federal and Indian leases represented 16.9

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[7]The 11,469 noncompetitive leases issued in 1983 fall into the following categories:

Program	*Public Domain*	*Acquired Lands*
Over the Counter	3,165	1,086
Simultaneous (Lottery)	6,020	1,198
Total	9,185	2,284

See U. S. Department of Interior, Bureau of Land Management, *Public Land Statistics 1983,* Table 66 at 124 (April 1983) (hereinafter *Public Land Statistics).*

[8]*See Public Land Statistics,* Table 67 at 126.

[9]*See Public Land Statistics,* Table 69 at 131.

[10]See U.S. Department of Interior, Minerals Management Service, *Mineral Revenues: The 1983 Report on Receipts from Federal and Indian Leases,* Table 25 at 68 (1984) (hereinafter *Mineral Revenues).*

percent to total United States production. In 1983, it represented 30.6 percent of such total production.[11]

The noncompetitive lease program is also a significant source of federal revenues. The Bureau of Land Management receipts for fiscal year 1983 included $908,574,130 from bonuses, rents, and royalties from oil and gas leases. This figure represents 76% of the total revenues to the BLM in 1983.[12] Approximately 75% of those revenues were realized from the noncompetitive program at issue in this case. Thus, any decision that threatens the certainty of title of these noncompetitive leases has the potential of disrupting a significant percent of the present and future oil and gas production.

Despite the current role of the noncompetitive lease program in the development of domestic petroleum reserves, the possibility of a challenge to other noncompetitive leases on the basis of the *Arkla Exploration Co.* decision may discourage future drilling. It is equally possible that a lessee would be reluctant to commit the capital for production, if there are doubts about the lease title. Indeed, Congress recognized long ago that the certainty of lease title was a necessary incentive for the industry to find and develop oil.

Other courts have recognized the importance of upholding the continuing validity of a lease, if it has been

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[11]*See Mineral Revenues,* Table 25 at 68.

[12]*See Public Land Statistics* at 194.

issued in accordance with the law.[13] In *Pan American Petroleum Corp. v. Pierson,* 284 F.2d 649, 655 (10th Cir. 1960), the court stated:

> It is common knowledge that exploration for oil and gas is costly. The drilling of wells requires substantial financial risks and the expense of putting those wells on production and of marketing the product is burdensome. If the continued existence of the granted leasehold estate is dependent upon the fluctuating policies of governmental departments uninhibited by any limitations upon time of action, the value of federal oil and gas leases as a title basis for oil and gas development is greatly diminished if not practically destroyed. No prudent operator would be willing to accept the financial risks if he were subject to ouster because of some administrative decision based upon improper conduct of an assignor occurring at some distant time in the past . . . Certainty of title is an elementary prerequisite for the sound development of any mineral resource.

Id. at 655.

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CONCLUSION

The decision of the Eighth Circuit clearly rewrites the definition of a KGS in the noncompetitive leasing program. By also holding that the Department of Interior's

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[13]The Tenth Circuit in *Pan American Petroleum Corp. v. Pierson,* 284 F.2d 649 (10th Cir. 1960) held that the lease assignee could not lose the lease for fraud perpetrated by the assignor before the lease was assigned. While this Court granted the petition for certiorari in *Boesche v. Udall,* 372 U.S. 472 (1963), to resolve an apparent conflict in the circuits, the holding did not reverse the Tenth Circuit's decision.

definition violated the Mineral Leasing Act of 1920, the decision raises questions about the certainty of lease title for noncompetitive leases that were issued under the disapproved definition and future noncompetitive leases. By making lease title uncertain, this decision will adversely affect a significant segment of the nation's onshore petroleum production and exploration industry. The door has been opened to untimely challenges and future commitments of capital are made risky and will not be expended until this issue is resolved. Therefore, Amicus urges this Court to grant the writ.

Respectfully submitted,

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October 1, 1984